

# A Comparison of the Competitiveness of the Automobile Industry in China and South Korea on the Basis of Porter's Diamond Model

## Topic and Research Question

China has become the largest automobile market in the world in 2013 and the market is still growing. Foreign car makers turn to the Chinese market for economic growth and profit. However the majority of cars sold in China are foreign cars. And despite growing car production, the car export remains relatively low.

South Korea's car makers on the other hand have achieved a remarkable success over the past decades. Hyundai and Kia were the 4th largest car maker in the world in 2012, are import car exporters in South Korea and internationally known brands.

While South Korea's car makers have become successful internationally, China's car makers are of much less importance.

This thesis aims to compare the competitiveness of China's and South Korea's automobile industry by answering the following research questions:

- How competitive are the automobile industries in China and South Korea?
- Is the Chinese automobile industry ready to compete with South Korea's? And has it the same beneficial (and potential) national environment necessary to achieve the same success story as the Korean automobile industry?
- How strong is governmental influence on the automobile industry in China and South Korea?
- How do multinational enterprises affect the Chinese and Korean automobile?

The topic is relevant for foreign car makers and suppliers to evaluate their Chinese and Korean competitors, to understand local markets and to develop strategies to remain successful and competitive against them in these markets.

## State of the Art

Due to China's growing economic importance, the automobile market has received much attention in research and public media alike. However, China is mostly seen as an important export market for foreign carmakers. Chinese car makers have received less attention from public media and science in the past. It is only lately with the beginning of Chinese brands emerging in Europe that they have been receiving more attention. The situation regarding South Korea's automobile sector is similar. The presence and the success of Korean brands in the automobile and electronics sector like Hyundai, Kia, Samsung and LG,

have led to more attention in public media and scientific research. But South Korea's car market has received less attention from scientists. The focus of research regarding South Korea has been on industrialization or on the role of government up to the Asian financial crisis. Porter's Diamond Model has been used to examine the competitiveness of different industries in various countries, including China's automobile industry. However, scientific papers on the automobile sector in both countries – especially on the past 10 years – are much rarer.

## Methodology and Approach

In order to answer the research questions, the thesis uses Michael Porter's Diamond Model as a foundation. The diamond model helps to explain why some nations are successful in international competition and how they gained a competitive advantage in a particular industry, whereas other nations have failed to achieve success. The model consists of six determinants, which influence each other and create an environment in which companies develop, operate and compete. These determinants are:

Factor conditions (natural resources, infrastructure), Demand Conditions of domestic customers, Related and Supporting Industries, Firm Strategy and Rivalry, Government policies and Chance.

Build upon Porter's Diamond Model is the Double Diamond Model that was proposed by Rugman and D'Cruz in order to address additional factors like international demand or multinational companies.

## Main Facts

China has become the largest car producer in the world, producing 18 million cars in 2013. However, despite the importance of China as a car producer, its relevance as a car exporter remains low as the vast majority of cars are produced to satisfy domestic demand. South Korea on the other hand is the fifth largest car producer in the world with 4 million cars produced in 2013. But in contrast to China, South Korea's car makers export a large share of their products.

Both China and South Korea provide their industries with a good infrastructure, skilled employees and R&D capabilities. In addition, China is the dominant supplier of rare earth minerals and the average wage in the automobile sector is lower than in South Korea. However, the infrastructure in Central and Western China falls behind the well-developed East and

countrywide, Chinese students perform only average in education, well behind South Korean students.

Regarding Demand Conditions, Chinese car makers can benefit from a large and still growing market with average sophisticated customers. However, demand for Chinese cars in the domestic and international markets is shrinking and the customers in the main export markets are less sophisticated. South Korea's domestic car market is much smaller than China's but the local customer are more sophisticated and South Korea's car makers still dominate their domestic market while Chinese car makers are losing market share to foreign competitors. Further, South Korea's car makers are successfully competing in international markets with sophisticated customers.

With regard to the role of related and supporting industries, the contrast between China and Korea is quite strong. The industries in China are very fragmented and mainly consist of smaller companies that produce less sophisticated goods and conduct little R&D themselves. Chinese companies try to compensate for this by acquiring foreign companies. South Korea's related and supporting industries on the other hand are quite successful with high R&D capabilities and the production of highly sophisticated goods that they sell internationally. Further, South Korea's car makers often rely on supporting companies within the chaebol network which established strong connections between car maker and supplier.

China's domestic industry is still dominated by large state-owned enterprises. However, private companies have emerged as well and achieved some success. Both, state-owned enterprises and private companies face a high degree of competition in their domestic market and the market share of Chinese brands is at an all-time low. The situation is different in South Korea. South Korean car makers still dominate their domestic market but the market share of foreign brands is increasing. And in contrast to many Chinese companies, South Korea's car makers focus on competing internationally and are quite successful with this approach, even in developed markets with a high degree of competition.

The government is an important factor in China and South Korea. In China, the state-owned companies have preferable access to capital, technology, raw materials, government protection and support through joint ventures with foreign companies. South Korea's government used to be very protective and supported its industry in the early stages of development. However, after the Asian Financial crisis governmental influence was reduced through a liberalization policy. Nevertheless, the government remains an important

factor, as it tries to steer the development of the industry in certain branches through financial incentives.

## Results

The thesis shows that the Korean automobile industry is very competitive while China's industry is far less so. Despite several improvements over the past decade, China's automobile industry cannot compete with its South Korean rivals yet. Government influence in China is far stronger than in South Korea as the Chinese governments protects and supports its industry to a much higher degree.

Despite some factors like a well-developed infrastructure, a large domestic market and high degree of competition that have a positive effect on the competitiveness of China's car makers, other factors like a low level of R&D, low degree of exports and the dependence on government support and joint ventures with foreign car makers have a negative impact on industry competitiveness.

Multinational companies are in China mainly to gain access to the large domestic market and conduct little R&D locally. In South Korea the situation is different. While Samsung Motors mainly supplies the local market, GM Korea – formerly Daewoo – has become a successful exporter.

South Korea's car makers are more competitive due to a high degree of R&D and an export oriented strategy. This is why this thesis comes to the conclusion that South Korea's automobile industry will continue to be as successful as it is today for the next few years.

## References

All references can be found in the full version of the MA thesis available at <http://othes.univie.ac.at/>

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